

Pillar 3 Disclosures **2009**

Most trusted
savings provider

Source: Marketing Sciences (March 2009)*



Proud to be a building society

Contents

1	Overview.....	5
1.1	Background	5
1.2	Basis and Frequency of Disclosures.....	5
1.3	Location and Verification.....	5
1.4	Scope	5
2	Risk Management.....	6
2.1	Group Risk Management Framework	6
2.2	Risk Appetite	6
2.3	Risk Management Policies.....	7
2.4	Board and Risk Management Committee Structure	8
2.5	Coverage of risks	8
3	Capital Resources	10
3.1	Total Available Capital.....	10
3.2	Tier 1 Capital	10
3.3	Tier 2 Capital	11
3.4	Solo consolidation	11
4	Capital Adequacy	12
4.1	Capital Management	12
4.2	Internal Capital Adequacy Assessment Process	12
4.3	Minimum Capital Requirement: Credit Risk	13
4.4	Minimum Capital Requirement: Pillar 1	13
5	Credit Risks	14
5.1	Credit Risk Overview.....	14
5.2	Retail Credit Risk.....	16
5.3	Commercial Credit Risk.....	18
5.4	Treasury Credit Risk.....	19
5.5	Impairment Provisions.....	21
5.6	Credit Risk Concentrations	23
5.7	Credit Risk Mitigation	24
5.8	Credit Derivatives.....	25
5.9	Securitisation.....	25
5.10	Counterparty Credit Risk.....	26
5.11	Credit risk model performance	27
5.12	Model Approvals & Validation	27
6	Market Risks.....	28
6.1	Market Risk Overview	28
6.2	Interest Rate Risk.....	28
6.3	Foreign Exchange Risk	29
6.4	Other market risks.....	29
7	Operational Risk	30
	Glossary of terms.....	33

* Source: Marketing Sciences (March 2009), respondents answering on which financial provider they would most trust with their savings.

Tables

Table 1: Total Available Capital.....	10
Table 2: Minimum capital requirement for credit risks.....	13
Table 3: Total minimum Pillar 1 capital requirement	13
Table 4: Credit risk exposures.....	14
Table 5: Geographical distribution of credit risk exposures.....	15
Table 6: Residual maturity of credit risk exposures.....	15
Table 7: Prime retail mortgage exposures under IRB	16
Table 8: Qualifying revolving retail exposures under IRB	17
Table 9: Other retail (unsecured lending) exposures under IRB.....	17
Table 10: Commercial lending by industry sector under the Standardised approach.....	18
Table 11: Internal default grades mapped to external ratings.....	20
Table 12: Central governments & central banks under Foundation IRB.....	20
Table 13: Institutions under Foundation IRB	21
Table 14: Corporates under Standardised	21
Table 15: Past due loans and provisions for impaired exposures.....	22
Table 16: Movement in impaired provisions.....	23
Table 17: Aggregate exposure to purchased securitisation positions.....	25
Table 18: Exposures to counterparty credit risk for derivative contracts.....	26
Table 19: Interest rate risk exposures	29
Table 20: Foreign exchange exposure	29

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Certain statements in this Pillar 3 Disclosure document are forward looking. Although Nationwide believes that the expectations reflected in these forward-looking statements are reasonable, we can give no assurance that these expectations will prove to be an accurate reflection of actual results. Because these statements involve risks and uncertainties, actual results may differ materially from those expressed or implied by these forward-looking statements.

We undertake no obligation to update any forward-looking statements whether as a result of new information, future events or otherwise.

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1 Overview

1.1 Background

The European Union Capital Requirements Directive came into effect on 1 January 2007 introducing consistent capital adequacy standards and an associated supervisory framework in the EU based on the Basel II Accord. The Directive is enforced in the UK by way of rules introduced by the Financial Services Authority (“the FSA”). Among them are disclosure requirements known as “Pillar 3” which apply to banks and building societies. These are designed to promote market discipline through the disclosure of key information about risk exposures and risk management processes.

In May 2008, the FSA granted Nationwide permission to use an Internal Ratings Based (IRB) approach to credit risk and capital management. The disclosures in this document are based on IRB approaches for certain portfolios and Standardised for the remainder of credit risks, and Standardised for operational risk as detailed in the capital management section (4.1).

1.2 Basis and Frequency of Disclosures

This document sets out the 2009 Pillar 3 Disclosures for Nationwide. These disclosures have been prepared solely to give information on the basis of calculating Basel II capital requirements and on the management of risks faced by the Group in accordance with the rules laid out in BIPRU Chapter 11. The disclosures may differ from similar information in the Annual Report and Accounts 2009 prepared in accordance with International Financial Reporting Standards (‘IFRS’); the information in these disclosures may therefore not be directly comparable with that information.

Unless otherwise stated, all figures are as at 4 April 2009 our financial year-end. Comparative figures for 2008 have only been included for the overall capital position. This is because Internal Ratings Based (IRB) approaches are used for credit risks in 2009 rather than Standardised in 2008.

Pillar 3 Disclosures will be issued on an annual basis and published as soon as practicable after the publication of the Annual Report and Accounts.

1.3 Location and Verification

These disclosures have been reviewed by the Group’s Audit Committee and the Group Risk Committee, and are published on the Group’s corporate website (www.nationwide.co.uk).

All figures disclosed within this document have been subject to internal verification. These disclosures have not been externally audited and do not constitute any part of the Group’s financial statements.

1.4 Scope

Nationwide is an EEA parent institution that is regulated by the FSA. The Basel II Framework therefore applies to Nationwide and its subsidiary undertakings (together, the “Group”). The Group also includes the business combinations that have occurred in the financial year to 4 April 2009 from the mergers with Derbyshire and Cheshire building societies, and assets and liabilities acquired from the Dunfermline Building Society (together, the “regional brands”).

There is a requirement to calculate and maintain regulatory capital ratios on both a Group basis and on a “solo consolidation” basis. However, there are no differences between the basis of consolidation of the Group for accounting and prudential purposes. The principal subsidiaries included under solo consolidation are:

• The Mortgage Works (UK) plc	• E-Mex Home Funding Limited
• UCB Home Loans Corporation Limited	• Nationwide Trust Limited
• Derbyshire Home Loans Limited	• Nationwide Syndications Limited

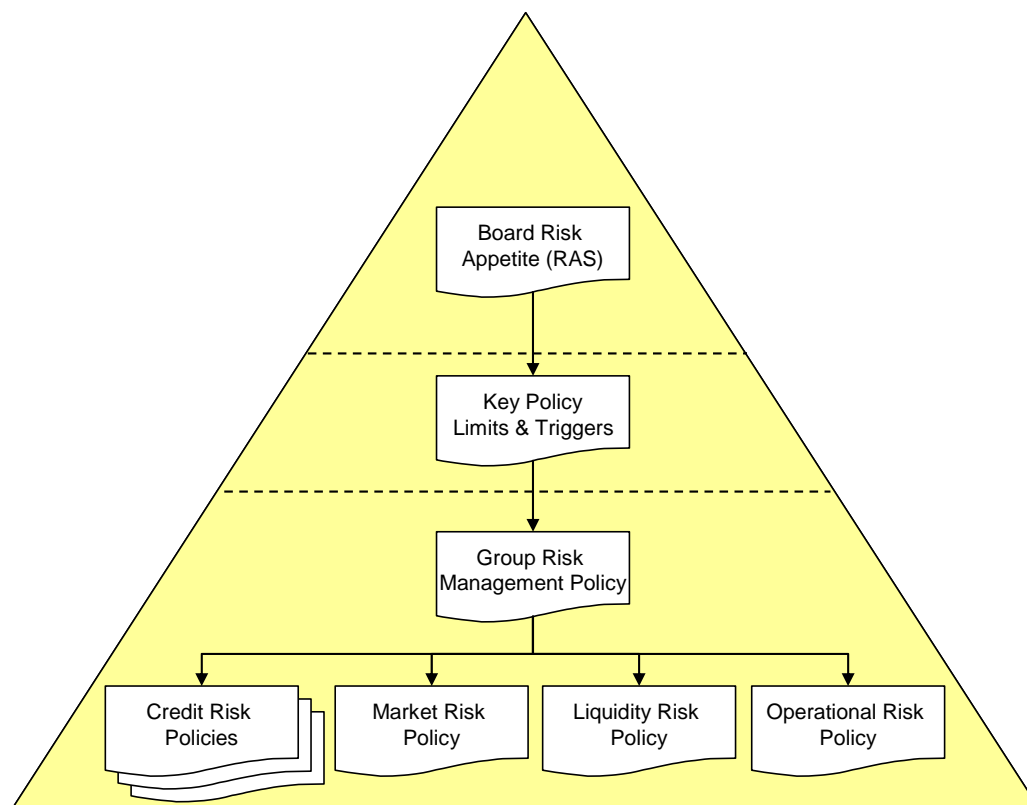
All of the Group’s subsidiaries are included in the Pillar 3 disclosures. Nationwide International Limited is regulated by the Isle of Man Financial Supervision Commission and has its own regulatory capital requirement. With that exception, the Group does not foresee any practical or legal impediments to the transfer of capital resources or the repayment of liabilities within the Group. Full details of the principal subsidiary undertakings are included in Note 22 to the Annual Report and Accounts.

2 Risk Management

2.1 Group Risk Management Framework

Nationwide operates within a comprehensive Group Risk Management Framework (GRMF) which comprises the following:

1. The Group Risk Appetite Statement (RAS) which is approved by the Board.
2. Key policy limits, triggers and mandates owned by the Board.
3. An overarching Group Risk Management Policy approved by the Board.
4. Detailed Risk Management Policies for specific risks approved by risk committees with delegated powers.
5. The adoption of the “Three Lines of Defence” approach to managing the risks.



The framework interacts with key processes of corporate management which the Board oversees:

- Corporate Plan.
- Internal Capital Adequacy Assessment Process (ICAAP).
- Stress Testing.

2.2 Risk Appetite

Nationwide is the custodian of its members' long-term financial interests. As a mutual organisation with no shareholders, the Board is prudent when deciding upon its appetite for risk relative to its banking peers, in order to take a long-term view of value creation. As such, the Board has agreed to adopt an overall low Risk Appetite, expressed in terms of the following eight categories:

- | | |
|--------------------|---------------------|
| • Profitability | • Return on Capital |
| • External Rating | • Liquidity |
| • Solvency | • Funding |
| • Economic Capital | • Asset quality |

The Board owns, sets and monitors key policy limits and triggers for these categories that provide the context for the detailed risk management policies, limits and triggers. In addition, separate Key Risk Indicators are set and monitored for operational risk appetite.

2.3 Risk Management Policies

The Board has assessed that the Group's most significant risk categories are credit risk, market risk, liquidity and funding risk, and operational risk. For each of these, there are detailed risk management policies with specific limits and triggers, documented as follows:

Risk policy

For all material risks within Nationwide's Risk Profile the Board's approach to risk management is documented within a set of detailed risk management policies which are owned and approved by the relevant mandated risk committee, and are supported by comprehensive limits, triggers, and processes.

Risk measurement

Robust and discriminatory internal ratings systems and models are used to measure the Group's credit risk exposures. These have been developed and validated according to documented and approved model development policies and procedures. Similarly, appropriate quantitative and qualitative methodologies have been developed to measure the Group's other material risk exposures, in line with industry best practice.

Risk control

Control of the Group's current and future exposure to risk is managed by the imposition of increasingly granular limits, triggers and mandates, which are embedded within Risk Policy and set by the relevant policy-owning Committee. This provides a clear hierarchical structure for identifying and managing risk against Risk Appetite.

Risk mitigation

All credit risk exposures, whether fully performing or otherwise, are reviewed at least annually. Behavioural scoring techniques are used to measure retail exposures while for commercial and treasury exposures a comprehensive health check on the financial standing of the borrower or counterparty is carried out. Both methods enable the Group to assess whether the level of credit given to borrowers remains acceptable.

Business Streams responsible for all of the material risks within Nationwide's Risk Profile ensure that appropriate mitigation techniques are undertaken to minimise the Group's exposure to each risk type. Additionally, they are responsible for minimising losses arising from the materialisation of a risk. Credit risk mitigation is described in more detail in section 5.7.

Risk monitoring and reporting

Specialist risk support functions are responsible for measuring and reporting performance against capital targets, as well as the limits, triggers and mandates contained within the relevant Group Risk Policy Statements. Management information is provided to the risk committees and to the Group Risk Committee every month. Summary information is prepared for consideration by the Board quarterly.

At all levels of reporting, if past or future forecast business performance appears to have moved, or is likely to move, outside of agreed parameters, or there is a breach or near-breach of policy limits, the relevant committee will ensure that the most appropriate course of action is implemented. Thereafter, if the situation persists the matter will be escalated, ultimately to the Nationwide Board.

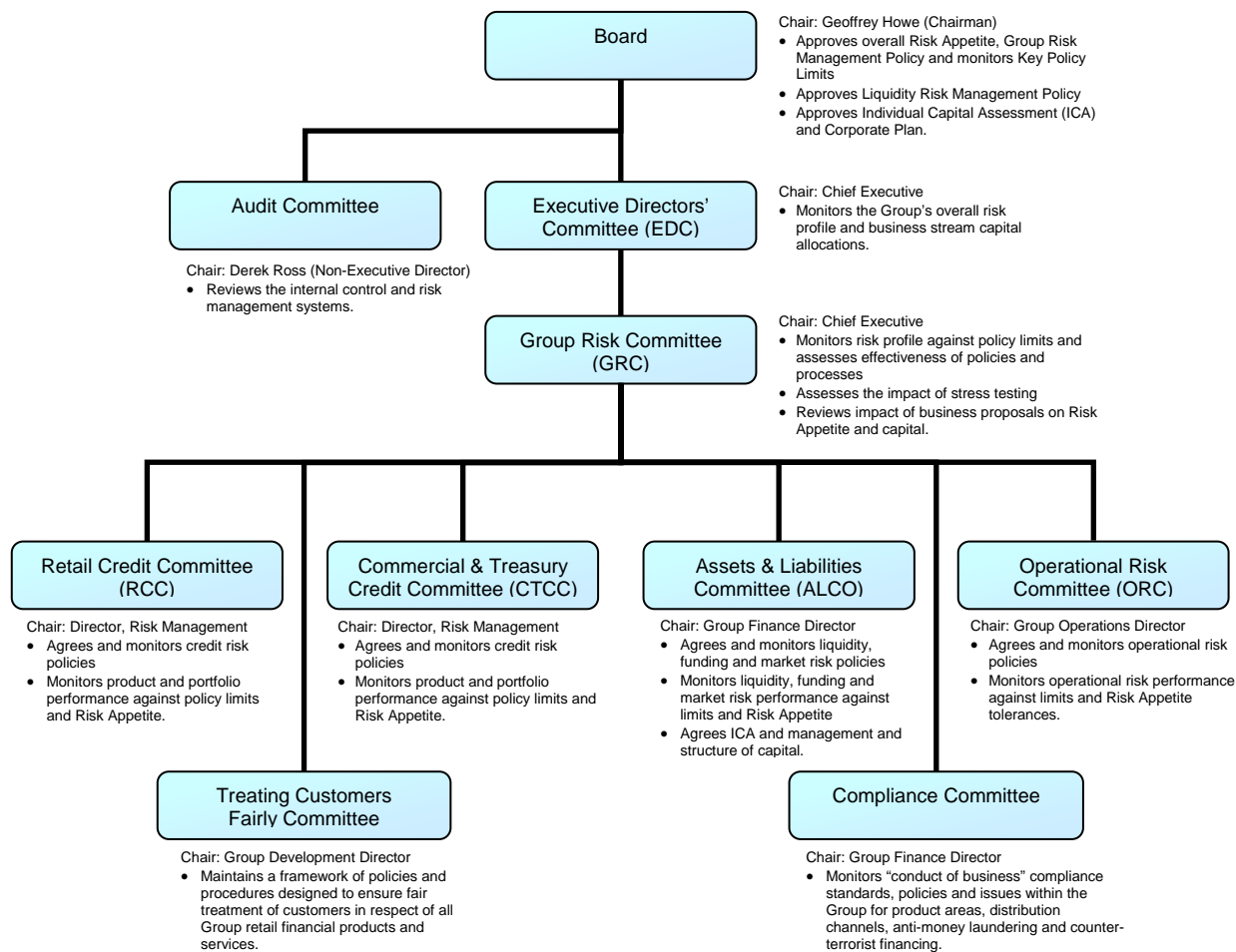
Risk governance & responsibilities

Governance and responsibilities for risk management is aligned to the Three Lines of Defence. Detailed responsibilities for risk committees and individuals in both Business Streams and Risk Management Division are set out in risk policies and include mandates where appropriate.

Risk committees ensure that risk policies and their terms of reference are reviewed annually or more frequently as required.

2.4 Board and Risk Management Committee Structure

The framework is supported by a well-established risk committee structure, summarised as follows:



Delegated committees are responsible for satisfying themselves that no material changes in risk levels and profiles have occurred or are planned. Where appropriate, they will prepare policy and strategy papers for agreement by the Group Risk Committee and/or the Nationwide Board. These papers will propose the appropriate scale, portfolio mix and/or desired return to fit with the Group's overall Risk Appetite.

The framework includes feedback mechanisms to ensure the continuing relevance and appropriateness of the governance, structure and risk monitoring metrics and escalation of issues.

2.5 Coverage of risks

Pillar 3 disclosures in this document cover credit risks (section 5), market risks (section 6), and operational risks (section 7); liquidity and funding risk falls outside the scope of these disclosures. Additional information regarding risk can be found in the 2009 Annual Report and Accounts (pages 99-109).

Responsibility for risk management (first line of the "Three Lines of Defence" model) lies with operational areas. Responsibilities for risk oversight and governance (the second line) lie with the specialist risk support functions in Risk Management Division (RMD) and powers delegated through the Group Risk Committee to specialist risk committees.

Responsibilities for the Group's main risks have been allocated as follows:

Key Risks	FIRST LINE	SECOND LINE	
	Risk Management	Risk Oversight (RMD)	Risk Governance ¹
Credit Risk			
• Retail credit risk	Retail Lending	Retail Credit Risk	Retail Credit Committee
• Commercial credit risk	Commercial Lending	Commercial & Treasury Credit Risk	Commercial & Treasury Credit Committee
• Treasury credit risk	Treasury Division	Commercial & Treasury Credit Risk	Commercial & Treasury Credit Committee
Market Risk	Treasury Division	Market Risk	Assets & Liabilities Committee
Operational Risk	All business areas	Operational Risk Unit	Operational Risk Committee
Liquidity and Funding Risk	Treasury Division	Market Risk	Assets & Liabilities Committee

¹ Oversight of all risk governance committees is provided by the Group Risk Committee.

First line of defence: senior management responsibilities

All Business Stream managers are responsible for managing business performance in line with the Group's overall Risk Appetite (per the Group Risk Management Framework described above). This requires them to manage their areas in line with operational performance targets and objectives cascaded from the Group's Corporate Plan, capital limits set within its Capital Plan, and risk exposure limits set within Group Risk Policies.

Second line of defence: risk committees

All risk committees have Board-mandated responsibility to: monitor business performance against Risk Appetite; to set, monitor and report on risk policy and methodology; and to challenge the risk management approach undertaken for their specific risks.

Second line of defence: specialist risk support functions

Specialist risk functions within Risk Management Division support the Board-mandated risk committees to fulfil their delegated responsibilities in respect of risk governance. These functions cover each of the significant categories of risk, namely retail, commercial and treasury credit risk, market risk, liquidity and funding risk, and operational risk, and play a major role in supporting the operational areas to manage their risks effectively on a day-to-day basis.

In addition, a Risk Analysis & Capital Planning function sits alongside the specialist risk support functions and is responsible for developing and maintaining the risk and capital management frameworks within which the entire Group operates.

All of the functions within Risk Management Division are mandated to carry out their responsibilities by the Board through the Group Risk Committee.

Third line of defence: Internal Audit

Group Internal Audit independently reviews the first and second lines of defence to provide objective assurance as to the adequacy and effectiveness of internal controls across the business. A risk-based programme of work is undertaken which is designed to provide appropriate coverage of the key business risks and processes. The Audit Committee approves the Annual Audit Plan and receives regular reports on the results of audit work.

3 Capital Resources

3.1 Total Available Capital

At 4 April 2009 and throughout the financial year, the Group complied with the capital requirements that were in force as set out by the FSA. The Group's Internal Ratings Based (IRB) Waiver Application was approved by the FSA in May 2008 with subsequent confirmation from the FSA that Nationwide has cleared the conditions required to use its IRB models to calculate capital requirements.

The following table shows the breakdown of the total available capital on the IRB basis for the Nationwide Group as at 4 April 2009 (2008 figures calculated on the Standardised basis):

Table 1: Total Available Capital

	Group		Solo	
	2009 £m	2008 £m	2009 £m	2008 £m
Tier 1				
General reserve	6,234	6,303	5,992	6,097
Permanent Interest Bearing Shares (PIBS)	1,526	1,245	1,526	1,245
Pension fund deficit adjustment	167	19	167	19
Intangible assets	(211)	(137)	(211)	(137)
Deductions ¹	(186)	(6)	(186)	(6)
Material holdings in non-solo consolidated subsidiaries ²	-	-	(16)	(5)
	7,530	7,424	7,272	7,213
Tier 2				
Revaluation reserve	69	121	69	121
Subordinated debt	2,233	1,743	2,233	1,743
Collective provisions for impairment	60	192	60	192
Deductions ¹	(186)	(6)	(186)	(6)
Material holdings in non-solo consolidated subsidiaries ²	-	-	(16)	(5)
	2,176	2,050	2,160	2,045
Qualifying holdings in non-solo consolidated subsidiaries ³	-	-	(409)	(408)
Total capital	9,706	9,474	9,023	8,850

¹ Certain deductions from capital are required to be allocated, 50% to Tier 1 and 50% to Tier 2 capital. Deductions are subject to different treatment under IRB in respect of net expected loss over accounting provisions and certain securitisation positions. These are calculated in accordance with FSA guidance.

² Under solo consolidation material holdings are excluded from capital and deducted equally from Tier 1 and Tier 2.

³ Under solo consolidation, qualifying holdings are excluded from capital and deducted to calculate total capital.

3.2 Tier 1 Capital

Tier 1 capital comprises:

- General reserve.
- Permanent Interest Bearing Shares (PIBS).
- Adjustments as required by the rules governing capital resources.

The general reserve represents the Group's accumulated accounting profits, including gains from the business combinations with Cheshire and Dunfermline, as well as adjustments for pensions and property disposals.

PIBS are unsecured, deferred shares and rank behind the claims of all subordinated noteholders, depositors, creditors and investing members of Nationwide. Further details about PIBS are provided in Note 37 to the 2009 Annual Report and Accounts.

The Group has no "innovative" Tier 1 instruments.

Adjustments are required by the rules governing capital resources:

- An adjustment is made to Tier 1 capital in respect of the Group's pension obligations. For accounting purposes, the present value of obligations less the fair value of plan assets in respect of the Nationwide Pension Fund ("the Fund") is included as a liability and hence deducted from the general reserve. For capital purposes this amount is added back to the Group's capital position; instead, a deduction is made for the additional funding that is expected to be paid to the Fund over the next 5 years. At 4 April 2009, £167m had been added back to capital in this regard which represents the aggregate of this adjustment.
- An adjustment is also made in respect of intangible assets. For accounting purposes, items including computer software, other intangibles resulting from business combinations, and goodwill are capitalised as intangible fixed assets where they meet certain criteria. Intangibles are deducted from capital under the regulatory rules; at 4 April 2009 £211m had been deducted from capital in respect of intangible assets.
- Deductions are also made under Basel II in respect of expected loss, where it exceeds accounting provisions for IRB exposures, and certain securitisations (£372m) split equally between Tier 1 and Tier 2.

3.3 Tier 2 Capital

Tier 2 capital comprises:

- The Group's property revaluation reserve.
- Qualifying subordinated notes.
- Collective impairment allowance (for exposures treated on the Standardised basis).
- Adjustments as required by the rules governing capital resources.

Subordinated notes are unsecured and rank behind the claims of all depositors, creditors and investing members (other than holders of PIBS) of the Society. More details of the subordinated notes are included in Note 36 to the 2009 Annual Report and Accounts.

Adjustments are required by the rules governing capital resources:

- Deductions are made under Basel II in respect of expected loss, where it exceeds accounting provisions for IRB exposures, and certain securitisations (£372m) split equally between Tiers 1 and Tier 2.

Under FSA rules, qualifying subordinated notes cannot exceed 50% of the total of Tier 1 capital, and Tier 2 capital cannot exceed Tier 1 capital.

3.4 Solo consolidation

Under the solo consolidation basis, deductions are required in respect of material holdings in subsidiaries that are excluded from solo consolidation. Material holdings represent shares and any other interest in the capital of an individual credit institution or financial institution where they exceed 10% of the share capital of the issuer. A deduction of £32m is made for material holdings allocated evenly between Tier 1 and Tier 2 capital.

In addition, qualifying holdings in subsidiaries are excluded from solo consolidation (£409m); under the rules these are deducted before the total of Tier 1 and Tier 2 capital to give the final capital position for the Group. A qualifying holding is a direct or indirect holding in a non-financial undertaking which represents 10% or more of the capital or of the voting rights which makes it possible to exercise a significant influence over the management of that undertaking.

4 Capital Adequacy

4.1 Capital Management

Nationwide manages its capital resources in excess of regulatory requirements. Capital is monitored on a monthly basis against the capital plan and supported by a range of limits and triggers that ensure that capital continues to be within the Board's risk appetite. In addition to calculating the minimum Capital Resource Requirement (CRR) as required under BIPRU rules, the Group uses an economic capital framework to support the management of its capital requirements. The CRR covers all Pillar 1 risks (credit risk, operational risk and market risk).

Credit risk

The Group has adopted Internal Ratings Based (IRB) approaches for certain credit risk portfolios following FSA approval in May 2008. The scope of our Internal Ratings Based permission is as follows:

Retail IRB	Society prime mortgages ¹ , unsecured lending (personal loans), and qualifying revolving credit risks (FlexAccount and credit cards).
Foundation IRB	Treasury exposures (excluding corporates).

All other credit risks adopt the Standardised approach. The more significant credit risk portfolios currently using the Standardised approach (commercial lending, Private Finance Initiatives, prime retail mortgages from the regional brands, and specialist retail mortgage lending) will migrate to IRB approaches under a rollout plan.

Market risk

Market risk for the Group arises from foreign exchange risk under Pillar 1 due to foreign currencies in the banking book. The Foreign Exchange Position Risk Requirement (FX PRR) charge is the amount of regulatory capital required to cover the risk of losses on open foreign currency positions due to movements in foreign exchange rates. This is calculated in accordance with the FSA Handbook. Other interest rate risks are not included in regulatory capital under Pillar 1 as the Group does not have a trading book.

Operational risk

The Standardised approach is adopted for operational risk.

Reporting

Capital is reported monthly in the Board Performance Pack. More detailed reports of capital and risk, including information by Business Stream, are considered monthly by the Group Risk Committee and the Capital Management Working Group (CMWG), a sub-committee of the Assets and Liabilities Committee (ALCO). Specific reports of capital by Business Stream are also included in the monthly packs of the risk committees as appropriate.

4.2 Internal Capital Adequacy Assessment Process

The Group undertakes an Internal Capital Adequacy Assessment Process (ICAAP) which is an internal assessment of its capital needs for Pillar 2 purposes. This internal assessment considers risks included in the Pillar 1 CRR as well as other risks not included in Pillar 1. The ICAAP is performed annually or more frequently should the need arise.

The outcome of the ICAAP is presented in an Internal Capital Assessment (ICA) document covering the Group and its subsidiaries. The ICA covers all material risks to determine the capital requirement over at least a three-year horizon, and takes account of severe economic stresses to satisfy the regulatory requirements and the effect of these on capital. Risks which cannot be mitigated effectively by capital (e.g. liquidity risk) are identified and described within the ICA.

The ICA is presented to CMWG, ALCO and the Board (with whom ultimate responsibility lies) for challenge and approval. The FSA has assessed our ICA and set Individual Capital Guidance (ICG) for the Group on an IRB basis which came into effect from May 2009.

¹ Prime mortgages originated by Nationwide and Portman only; prime mortgages from the regional brands are treated as Standardised.

4.3 Minimum Capital Requirement: Credit Risk

The following table shows Nationwide's overall minimum capital requirement for credit risk at 4 April 2009. Comparisons with 2008 are not included as credit risk was on a Standardised basis. The Solo figures are slightly higher than the Group due to loans from the Group to subsidiaries that are not solo-consolidated.

Table 2: Minimum capital requirement for credit risks

	Group £m	Solo £m
Internal Ratings Based (IRB) exposure classes		
Central governments & central banks	240	240
Institutions	354	354
Retail mortgages (prime secured against residential property)	333	333
Qualifying revolving retail ¹	178	178
Other retail (unsecured loans)	77	77
Securitisation positions	78	78
Non-credit obligation assets (fixed assets & other)	106	108
	1,366	1,368
Standardised (Std) exposure classes		
Regional governments & local authorities	3	3
Institutions	2	2
Corporates ²	161	208
Retail mortgages (secured against residential property) ³	666	666
Other retail	1	1
Commercial lending (secured against property)	1,324	1,324
Past due ⁴	143	143
Other	20	16
	2,320	2,363
Total credit risk minimum capital requirement	3,686	3,731

¹ Credit cards and current accounts (FlexAccount).

² Corporates includes Private Finance Initiatives (PFI) and other commercial lending.

³ Retail mortgages from regional brands and specialist mortgage lending.

⁴ Past due primarily relates to specialist mortgage lending and commercial lending.

4.4 Minimum Capital Requirement: Pillar 1

Nationwide's overall minimum Capital Resource Requirement (CRR) under Pillar 1 is calculated by adding the credit risk charge (section 4.3) to that required for market risk and operational risk. The following table shows the Group's CRR and capital resources surplus under Pillar 1 at 4 April 2009 (2008 figures calculated on the Standardised basis):

Table 3: Total minimum Pillar 1 capital requirement

	Group		Solo	
	2009 £m	2008 £m	2009 £m	2008 £m
Credit Risk (IRB)	1,366	-	1,368	-
Credit Risk (Standardised)	2,320	5,811	2,363	5,865
Market Risk (FX PRR)	3	3	3	3
Operational Risk (Standardised)	296	317	296	317
Capital Resources Requirement under Pillar 1	3,985	6,131	4,030	6,185
Capital resources (per Table 1)	9,706	9,474	9,023	8,850
Capital resources surplus over requirement	5,721	3,343	4,993	2,665

The total minimum capital requirements are not materially different on a Group or solo basis; the disclosures in the remainder of this document are therefore shown on a Group basis only.

5 Credit Risks

5.1 Credit Risk Overview

Introduction

Credit risk is defined as the risk that a borrower or counterparty fails to pay the interest or to repay the capital on a loan.

Risks arising from changes in credit quality, and the recoverability of loans and amounts due from counterparties, are inherent across most of the Group's activities. Adverse changes in the credit quality of borrowers or a general deterioration in UK economic conditions could affect the recoverability and value of the Group's assets and therefore its financial performance. Comprehensive risk management methods and processes have been established as part of the Group's overall governance framework to measure, mitigate and manage credit risk within the Group's Risk Appetite.

Exposure as shown in these credit risk disclosures is defined as Exposure at Default (EAD) under the definitions for regulatory capital purposes. This is an estimate of the expected utilisation of a credit facility and will be equal to or greater than the drawn exposure and exclude any credit risk mitigation.

Exposures

The credit risk exposures at 4 April 2009 and the averages for the year are summarised as follows:

Table 4: Credit risk exposures

	Average 2008/09 £m	4 April 2009 £m
Internal Ratings Based (IRB) exposure classes		
Central governments & central banks ¹	35,820	38,183
Institutions ¹	29,522	24,086
Retail mortgages (prime secured against residential property)	114,533	113,931
Qualifying revolving retail ²	7,847	8,002
Other retail (unsecured lending)	1,267	1,220
Securitisation positions	7,270	7,290
Non-credit obligation assets (fixed & other)	1,228	1,325
	197,487	194,037
Standardised exposure classes		
Regional governments & local authorities	39	38
Institutions	36	139
Corporates (excluding commercial loans)	649	585
Retail mortgages (secured against residential property) ³	18,354	22,553
Other retail	23	21
Commercial lending (including PFI) ⁴	22,519	22,830
Past due	905	1,533
Other	572	949
	43,097	48,648
Total	240,584	242,685

¹ Including repurchase agreements.

² Credit cards and current accounts (FlexAccount).

³ Retail mortgages from regional brands and specialist mortgage lending.

⁴ Commercial lending secured against property, Private Finance Initiatives, and other commercial lending.

The following tables show the geographical distribution and residual maturity of these exposures at 4 April 2009.

Table 5: Geographical distribution of credit risk exposures

	UK £m	Other European Countries £m	North America £m	Rest of the World £m	Total £m
IRB exposure classes					
Central governments & central banks	35,803	2,280	49	51	38,183
Institutions	6,910	13,508	2,494	1,174	24,086
Retail mortgages (prime secured against res. property)	113,931	-	-	-	113,931
Qualifying revolving retail	8,002	-	-	-	8,002
Other retail (unsecured lending)	1,220	-	-	-	1,220
Securitisation positions	2,634	2,303	2,125	228	7,290
Non-credit obligation assets (fixed & other)	1,325	-	-	-	1,325
	169,825	18,091	4,668	1,453	194,037
Standardised exposure classes					
Regional governments & local authorities	38	-	-	-	38
Institutions	122	1	-	16	139
Corporates (excluding commercial loans)	121	425	39	-	585
Retail mortgages (secured against residential property)	22,553	-	-	-	22,553
Other retail	21	-	-	-	21
Commercial lending (including PFI)	21,604	1,226	-	-	22,830
Past due	1,519	14	-	-	1,533
Other	867	40	39	3	949
	46,845	1,706	78	19	48,648
Total	216,670	19,797	4,746	1,472	242,685

Table 6: Residual maturity of credit risk exposures

	On demand £m	Up to 12 months £m	1-5 years £m	5-10 years £m	More than 10 years £m	Total £m
IRB exposure classes						
Central governments & central banks	-	31,447	1,925	2,763	2,048	38,183
Institutions	-	13,023	6,446	4,585	32	24,086
Retail mortgages (prime secured against res. property)	-	795	3,430	10,172	99,534	113,931
Qualifying revolving retail	8,002	-	-	-	-	8,002
Other retail (unsecured lending)	-	62	922	229	7	1,220
Securitisation positions	-	-	351	793	6,146	7,290
Non-credit obligation assets (fixed & other)	423	-	264	250	388	1,325
	8,425	45,327	13,338	18,792	108,155	194,037
Standardised exposure classes						
Regional governments & local authorities	-	-	21	13	4	38
Institutions	-	126	11	-	2	139
Corporates (excluding commercial loans)	-	94	199	292	-	585
Retail mortgages (secured against residential property)	-	172	1,270	8,046	13,065	22,553
Other retail	-	-	7	9	5	21
Commercial lending (including PFI)	-	377	1,652	2,169	18,632	22,830
Past due	-	29	96	270	1,138	1,533
Other	-	867	30	30	22	949
	-	1,665	3,286	10,829	32,868	48,648
Total	8,425	46,992	16,624	29,621	141,023	242,685

The maturity of exposures is shown on a contractual basis rather than the actual redemptions experienced by the Group or the Society, and does not take into account any instalments receivable over the life of the exposure. As a consequence actual maturity is likely to be materially different.

The Group is firmly committed to the management of credit risk in both its lending and Treasury market activities. For all its lending business the Group employs sophisticated credit scoring, underwriting and fraud detection techniques that support sound credit decision making and work to minimise losses. A proactive approach to the identification and control of loan impairment is maintained, with challenge and oversight provided by the Retail Credit Committee and the Commercial & Treasury Credit Committee with further oversight by the Group Risk Committee.

5.2 Retail Credit Risk

Prime mortgages², revolving retail (FlexAccount and credit card), and unsecured lending adopt the Retail IRB approach where Probability of Default (PD), Exposure at Default (EAD) and Loss given Default (LGD) are calculated using a rating system. Other retail portfolios are currently calculated on the Standardised basis.

The following table shows the Group's exposure for prime Society mortgages under IRB at 4 April 2009:

Table 7: Prime retail mortgage exposures under IRB

PD band %	EAD £m	Exposure Weighted Average LGD %	Exposure Weighted Average RWA %
0 - 0.019	29,380	6.1	0.9
0.02 - 0.029	37,646	8.7	1.3
0.03 - 0.049	21,441	11.6	2.3
0.05 - 0.099	13,184	13.5	4.2
0.10 - 0.49	5,981	19.2	10.5
0.50 - 0.99	1,282	19.1	24.8
1.00 - 2.99	1,210	10.9	32.3
3.00 - 9.99	533	11.6	71.8
10.00 - 19.99	272	9.4	84.4
20.00 - 99.99	436	9.8	77.2
100.00% (in default)	209	3.4	0.0
Commitments	2,357		3.8
Total	113,931		

The PD model for prime mortgages uses a hybrid rating system that combines Point in Time (PiT) grade distributions with conservatively-adjusted probabilities of default. The PiT grade distributions are mapped from the application scores, behavioural scores and arrears status. Each grade is assigned a conservatively-adjusted or long run average PD that is used in the capital calculation. The model allows ratings migration to occur dependent on the economic cycle.

Both LGD and EAD models calculate PiT and downturn estimates, the latter of which are fed into the capital calculation. LGD takes account of house price forecasts, collection costs adjusted for region, loan-to-value (LTV), external credit rating data and the likelihood of loss in the event of default to predict the loss on the property at the point of sale. The regulatory floor of 10% is applied when appropriate and any estimated recoveries after sale are not included. EAD takes account of balances and an adjustment to include the potential for additional months' interest prior to default.

Internal data covering the period back to the early 1990s has been used in the development of both PD and LGD models. This has been supplemented with industry data where appropriate.

² Prime mortgages originated by Nationwide and Portman; prime mortgages from the regional brands are treated as Standardised.

The following table shows the Group's exposure for qualifying revolving retail portfolios (FlexAccounts and credit cards) under Retail IRB at 4 April 2009:

Table 8: Qualifying revolving retail exposures under IRB

PD band %	EAD £m	Exposure Weighted Average LGD %	Exposure Weighted Average RWA %
0 - 0.29%	2,147	40.1	4.0
0.30 - 0.49%	2,619	44.7	9.7
0.50 - 0.99%	769	48.9	20.8
1.00 - 1.99%	974	52.4	34.9
2.00 - 9.99%	1,009	50.5	82.7
10.00 - 39.99%	355	57.1	147.5
40.00 - 99.99%	14	56.6	163.0
100.00% (in default)	115	58.6	0.0
Total	8,002		

The following table shows the Group's exposure for other retail (unsecured lending) under IRB at 4 April 2009:

Table 9: Other retail (unsecured lending) exposures under IRB

PD band %	EAD £m	Exposure Weighted Average LGD %	Exposure Weighted Average RWA %
0 - 0.99%	222	62.1	55.5
1.00 - 1.99%	483	62.1	77.1
2.00 - 5.99%	263	62.1	90.8
6.00 - 9.99%	107	62.1	99.2
10.00 - 19.99%	33	62.1	125.4
20.00 - 99.99%	18	62.1	167.1
100.00% (in default)	67	62.1	0.0
Commitments	27		79.2
Total	1,220		

The PD models for unsecured and revolving retail portfolios use rating systems that takes Point in Time (PiT) grade distributions of default and adjusts these to determine probabilities of default in a downturn. Key inputs to the PiT grade distributions are arrears status and behavioural or application scores. The adjustments result in long run average, 12-month PDs that are conservative estimates as to how accounts would be expected to perform over an economic cycle.

Both LGD and EAD models take PiT estimates that are adjusted to give downturn results to feed into the capital calculation. Statistical techniques are used to develop homogeneous pools across the unsecured portfolios. These models estimate average loss (percentage) of EAD over a recovery period that is specific to the particular product type, and take account of balances and limit utilisation for each pool, credits to accounts and account age.

Management of retail credit risks

Retail credit risks are managed in accordance with limits set out within the policy approved by Retail Credit Committee (and ratified by the Board). The policy sets out where specialist underwriting may be needed.

For residential mortgages, a combination of lending policy criteria, credit scoring (including behavioural scoring), policy rules and underwriting are used to make a decision on applications for credit. The primary factors considered are affordability, residential status, residential history, credit history, employment history, nature of income and loan-to-value (LTV). In addition, confirmation of borrower identity is obtained and an assessment of the value of the security being taken as collateral is carried out prior to granting a credit facility. When considering applications the primary focus is placed on the willingness and ability to repay.

Credit scoring is used to support the customer account management process in the following ways:

- To set customer maximum lending limits.
- To pre-determine lending limits for selected further advances.
- To determine account specific recommended limits and product types.
- To set shadow limits to manage unauthorised borrowing.
- To prioritise collections activity.

The maximum mortgage loan is calculated and expressed as a percentage of the vacant possession price or open market value, whichever is the lower; for re-mortgages the LTV is determined by the open market value. A range of LTV limits apply for new business across the mortgage portfolio as a whole and also at portfolio level (prime, specialist lending). Limits are also set for the concentrations of LTV bands.

No lending is undertaken based solely upon security provided by the value of the underlying assets, and the decision to lend rests with the Retail Credit Risk function in Risk Management Division. Once a mortgage application is made, the sales force has no bearing on the final decision. All mortgages are secured by way of a first legal charge against the property.

For unsecured products, similar lending policy criteria are used. Each of the unsecured portfolios has its own credit scoring models (including behavioural scoring), policy and underwriting rules to make decisions on applications for credit and to manage accounts. The factors used are attuned to the portfolio in question although affordability and credit history are considered in all areas. Accounts are subject to behavioural scoring every month.

Ongoing monitoring of all retail credit portfolios is undertaken by the Retail Credit Risk function in Risk Management Division. Reports are sent to the Retail Credit Committee and Group Risk Committee on a monthly basis. In the event that particular exposures show adverse features such as arrears, specialist lending teams will work with borrowers to resolve the situation.

5.3 Commercial Credit Risk

Nationwide's commercial lending activity is split between lending to private sector landlords and property investors, registered (and unregistered) social landlords, and funding projects originated under Private Finance Initiatives and Public Private Partnerships.

The following table provides an analysis of commercial lending exposure by industry sector (including past due) at 4 April 2009:

Table 10: Commercial lending by industry sector under the Standardised approach

	£m
Registered Social Landlords	8,062
Private Finance Initiatives (PFI) ¹	1,230
Property Finance lending:	
• Retail	4,094
• Office	3,139
• Residential	2,456
• Industrial and warehouse	2,183
• Leisure and hotel	955
• Owner occupier	997
• Other	214
Regional governments and local authorities (lease receivables)	38
Total	23,368

¹ PFI treated as unrated corporates

Commercial credit risks are managed in accordance with limits and asset quality measures which are set out in the policy approved by the Commercial & Treasury Credit Committee (and ratified by the Board). The policy places limits on business volumes as well as the sector, geography, size and seniority of exposures.

Reports are sent to the Commercial & Treasury Credit Committee and the Group Risk Committee on a monthly basis.

Lending decisions are based upon independent credit risk analysis supplemented by the use of expert judgement models which assess the obligor's likelihood of default. The output of these models is a borrower grade which maps to a long-run average, one-year probability of default. Borrower grades are reviewed at least annually, allowing identification of adverse individual and sector trends.

The Commercial & Treasury Credit Risk function in Risk Management Division has a level of delegated sanctioning authority and underwrites certain credit risks based upon an evaluation of model outputs and a qualitative overlay based on expert judgement. Factors taken into consideration are the borrower's experience, track record, financial strength, ability to repay, transaction structure and security characteristics. Large or high risk exposures are subject to further approval by the Commercial & Treasury Credit Committee and/or the Group Risk Committee. Consideration is also given to risk mitigation measures which will provide the Group with protection, such as third-party guarantees, supporting collateral and security, robust legal documentation, financial covenants and hedging.

To ensure that risks are appropriately priced, transactions are further assessed using an internal pricing model which takes into account capital utilisation and return on economic capital, as measured against a series of limits/targets disseminated from the Capital Plan.

Commercial portfolio asset quality monitoring is based upon a number of measures, including, economic capital, financial covenant monitoring, pricing movements and external input from rating agencies and other organisations. In the event that particular exposures begin to show adverse features such as payment arrears, covenant breaches or business trading losses, a full risk reappraisal is undertaken.

Where appropriate, a specialist recovery team will work with the borrower to resolve the situation. If this proves unsuccessful, the case will be subject to intensive monitoring and management procedures designed to maximise debt recovery.

5.4 Treasury Credit Risk

Treasury credit risks are managed in accordance with limits, asset quality measures and criteria set out within the policy approved by the Commercial & Treasury Credit Committee (and ratified by the Board). The policy also sets out powers which require higher levels of authorisation according to the size of the transaction or the nature of the associated risk.

Lending and investment decisions are made by applying a qualitative overlay adjustment to the outputs of a quantitative financial strength rating model, in order to reflect material changes in internal and external operating conditions that may not yet be reflected in the financials. The output from this process provides Nationwide with a long-term unsecured debt rating, comparable to Moody's. Once on book, all individual exposures are reviewed at least annually.

Treasury uses a number of risk mitigation techniques including netting and collateralisation agreements. Other methods (such as margining, credit breaks, compounding, termination and credit derivatives) are used periodically to mitigate the credit risk associated with particular transactions or group of transactions.

Ongoing asset quality monitoring is undertaken by Treasury and the Commercial & Treasury Credit Risk function in Risk Management Division. Reports are sent to the Commercial & Treasury Credit Committee and the Group Risk Committee on a monthly basis. Where necessary, exception reporting also takes place against a range of asset quality triggers including economic capital analysis.

Nationwide uses Standard and Poor's (S&P), Moody's and Fitch as External Credit Assessment Institutions (ECAIs) for treasury credit risk exposures. S&P is used for Sovereigns, Institutions, Asset Backed Securities, Covered Bonds and Corporates. Moody's is used for Sovereigns, Institutions, Covered Bonds and Asset Backed Securities. Fitch is used for Asset Backed Securities.

The Group's preference for a long-term rating for Institutions and Corporates is the senior unsecured rating. If this is unavailable, then counterparty ratings and deposit ratings are used to record the short-term rating or the commercial paper rating. The issue/note rating is used for Asset Backed Securities.

The issuer and issue credit assessments provided by ECAs are one of a number of considerations that form part of the credit assessment process. This process is documented within policy and is supported by comprehensive Treasury Credit procedures.

An Internal Ratings Based (IRB) model is used to determine Probability of Default (PD) for Treasury exposures (excluding corporates). Under Foundation IRB, standard regulatory parameters are used for Loss Given Default (LGD) and the conversion factor. The PD model for banks consists of two key elements – a statistically-driven quantitative financial strength rating and a qualitative overlay. For non-bank entities and investment banks, external ratings are substituted for the quantitative element.

The qualitative adjustment is applied to the calculated quantitative rating or external rating as appropriate to reflect material changes in internal and external operating conditions that may not yet be reflected in the financials or published external ratings. The adjustment also recognises any external support mechanisms that would take effect in the event of the counterparty encountering financial difficulties, environmental (external) factors and business environment (internal) factors.

The model generates a long-term, unsecured debt rating by combining these quantitative and qualitative factors. The output is a numerical rating ranging from 1 to 22, with grades 1 to 10 equating to investment grade status and grade 22 representing in default. The following table shows the mapping of internal default grades to external ratings at 4 April 2009:

Table 11: Internal default grades mapped to external ratings

Internal Default Grades	S & P ratings	Moody's ratings	Fitch ratings
1 – 3	AAA to AA	Aaa to Aa2	AAA to AA
4 – 6	AA- to A	Aa3 to A2	AA- to A
7 – 9	A- to BBB	A3 to Baa2	A- to BBB
10 – 12	BBB- to BB	Baa3 to Ba2	BBB- to BB
13 – 16	BB- to B-	Ba3 to B3	BB- to B-
17 – 22	CCC+ to D	Caa to C	CCC to D

The following table shows the exposure values associated with central governments and central banks under Foundation IRB including commitments at 4 April 2009. Repurchase agreements with the Bank of England are included in the EAD under internal default grades 1-3 which affects the exposure weighted average LGD.

Table 12: Central governments & central banks under Foundation IRB

Internal Default Grades	PD bands as at 04/04/2009 %	EAD £m	Exposure-weighted average LGD%	Average RWA %
1-3	0 - 0.03	38,127	26.5	7.8
4	0.031 - 0.04	0	-	-
5	0.041 - 0.05	0	-	-
6	0.051 - 0.07	0	-	-
7	0.071 - 0.1	56	45.0	19.8
8	0.101 - 0.2	0	-	-
9	0.201 - 0.3	0	-	-
10	0.301 - 0.5	0	-	-
11	0.501 - 0.75	0	-	-
12	0.751 - 2.0	0	-	-
13-21	2.001 - 99.999	0	-	-
22	100% (in default)	0	-	-
Total		38,183		

The following table shows the exposure values associated with institutions under Foundation IRB including commitments at 4 April 2009. Repurchase agreements are included in this table which affects the exposure weighted average LGD where appropriate.

Table 13: Institutions under Foundation IRB

Internal Default Grades	PD bands as at 04/04/2009 %	EAD £m	Exposure-weighted average LGD%	Average RWA %
1-3	0 - 0.03	6,295	23.9	8.4
4	0.031 - 0.04	1,104	32.4	11.7
5	0.041 - 0.05	8,701	35.7	17.9
6	0.051 - 0.07	4,267	45.0	25.2
7	0.071 - 0.1	2,007	43.4	27.2
8	0.101 - 0.2	865	40.4	35.2
9	0.201 - 0.3	280	45.0	44.2
10	0.301 - 0.5	4	45.0	65.9
11	0.501 - 0.75	399	5.3	12.4
12	0.751 - 2.0	5	45.0	111.1
13-21	2.001 - 99.999	83	45.0	120.0
22	100% (in default)	76	45.0	-
Total		24,086		

The following table shows the exposure values with each credit quality step for corporate treasury exposures under the Standardised approach at 4 April 2009:

Table 14: Corporates under Standardised

Credit Quality Step	Risk weight %	S & P ratings	Moody's ratings	Exposure Values £m
1	20	AAA to AA-	Aaa to Aa3	18
2	50	A+ to A-	A1 to A3	34
3	100	BBB+ to BBB-	Baa1 to Baa3	60
4	100	BB+ to BB-	Ba1 to Ba3	23
5	150	B+ to B-	B1 to B3	-
6	150	CCC+ and below	Caa1 and below	20
Unclassified	100	Unknown	Unknown	430
Total				585

Exposure values for equities are risk-weighted at 100% and included under Standardised "other" (see Table 4). Exposure values for Asset Backed Securities can be found in section 5.9.

5.5 Impairment Provisions

Assets held at amortised cost

The Group assesses at each balance sheet date whether, as a result of one or more events that occurred after initial recognition, there is objective evidence that a financial asset or group of financial assets are impaired. Evidence of impairment may include indications that the borrower or group of borrowers are experiencing significant financial difficulty, default or delinquency in interest or principal payments or the debt being restructured to reduce the burden on the borrower.

The Group first assesses whether objective evidence of impairment exists either individually for assets that are separately significant or individually or collectively for assets that are not separately significant. If there is

no objective evidence of impairment for an individually-assessed asset it is included in a group of assets with similar credit risk characteristics and collectively assessed for impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the carrying amount of the asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The resultant provisions have been deducted from the appropriate asset values in the balance sheets.

The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Group to reduce any differences between loss estimates and actual loss experience.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised the provision is adjusted and the amount of the reversal is recognised in the income statement.

Where a loan is not recoverable, it is written off against the related provision for loan impairment once all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of impairment losses recorded in the income statement.

Loans subject to collective impairment assessment and whose terms have been renegotiated are no longer considered to be past due or impaired but are treated as new loans after the minimum required number of payments under the new arrangements have been received. Loans subject to individual impairment assessment, whose terms have been renegotiated, are subject to ongoing review to determine whether they remain impaired or are considered to be past due.

The following table shows the past due loans and provisions for impaired exposures (equivalent to value adjustments) and charges to the income statement for the year ended 4 April 2009. For the purposes of this table, past due is defined as one day or over. The amounts shown as past due represent the full amount of the loan outstanding, not just the amount that is past due.

Table 15: Past due loans and provisions for impaired exposures

	Retail secured lending £m	Retail unsecured lending £m	Commercial lending £m	Total £m
Neither past due nor impaired	128,121	2,187	22,427	152,736
Past due:				
Up to 3 months	3,285	58	557	3,900
3 to 6 months	660	63	122	845
6 to 12 months	420	70	229	719
Over 12 months	143	37	21	201
Possessions	248	-	12	260
Subtotal	4,756	228	941	5,925
Outstanding balances	132,877	2,415	23,368	158,661
Provisions	120	143	207	470
Charge/(credit) for the year	91	114	189	394

Past due loans, impaired loans and provisions are all UK-based with the exception of £18m impairment charge relating to a portfolio of European commercial loans.

The following table summarises the movement during the year in impairment provisions:

Table 16: Movement in impaired provisions

	Individual Provisions £m	Collective Provisions £m	Total £m
Balance at 5 April 2008	11	201	212
Charge for the year	239	155	394
Write-offs	(18)	(126)	(144)
Recoveries	1	17	18
Unwind of discount	(4)	(6)	(10)
Balance at 4 April 2009	229	241	470

Further information on the charge to the income statement for provisions and more detailed analysis is included in Note 13 in the Annual Report and Accounts (pages 72-73).

During the year an impairment loss of £48 million in Group and Society (2008: Group and Society loss of £102 million) has been recognised in the income statement as a result of liquidity issues faced by a number of treasury investment securities. Total impairment losses on investment securities of £51 million also include £3 million relating to non Available For Sale assets.

Available For Sale assets

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets are impaired. If any such evidence exists for Available For Sale financial assets, the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised) is recognised in the income statement.

A subsequent decline in the fair value of an investment security classified as Available For Sale is recognised in the income statement when there is further objective evidence of impairment as a result of further decreases in the estimated future cash flows of the financial asset. Where there is no further objective evidence of impairment, the decline in the fair value of the financial asset is recognised directly in the Available For Sale reserve. If the fair value of an investment debt security classified as Available For Sale increases in a subsequent period, and the increase can be related objectively to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement to the extent of the increase in fair value.

As at 4 April 2009, over 99% of the liquidity portfolio is rated A or better (78% rated AA or above), and over 97% of the investment portfolio is rated A or better (76% rated AA or above).

5.6 Credit Risk Concentrations

For residential mortgages, LTV concentration limits are set within policy. Geographic concentration of risk is also monitored, but no specific parameters are deemed necessary for domestic lending. The Group operates across the whole of the UK with a bias towards the South-East of England reflecting a concentration of the market in that region and historically higher asset value growth trends. As at 4 April 2009 approximately 34% (2008: 36%) of residential exposures by account was concentrated in the South-East of England. By their nature, our residential mortgages and unsecured lending comprise a large number of intrinsically highly diversified small loans and have a low volatility of credit risk outcomes.

For commercial lending, exposure to each of the principal lending categories is monitored and total portfolio exposure constrained via a self-imposed cap set at 17.5% of Nationwide's total business assets. Limits are also set restricting the size of aggregate exposure to any single counterparty or group of closely-connected counterparties. Concentration of risk within the portfolio is monitored using indicators such as maturity, industry sector and geography, though specific limits are not normally imposed for UK-domiciled lending.

In terms of counterparty concentration, the largest single commercial customer, including undrawn commitments, represents only 1% (2008: 2%) of the commercial portfolio.

Policy limits have also been set to enable the management of treasury credit risk concentrations. These limits are actively monitored and relate to aggregate counterparty, country and asset class exposures.

5.7 Credit Risk Mitigation

The Group uses a wide range of techniques to reduce credit risk of its lending. The most basic of these is performing an assessment of the ability of a borrower to service the proposed level of borrowing without distress. However, the risk can be further mitigated by obtaining security for the funds advanced.

Residential mortgages

Residential property is the Group's main source of collateral and means of mitigating credit risk inherent in its residential mortgage portfolios. All mortgage lending activities are supported by an appropriate form of valuation using either an independent firm of valuers (except historic low LTV re-mortgage cases valued without independent valuation), indexed valuation (further advances) or by Automatic Valuation Model subject to business rules and confidence levels.

All residential property must be insured to cover property risks, which may be through a third party. Additional protection is also afforded to borrowers through optional payment protection insurance.

Commercial

Commercial property is the Group's main source of collateral and means of mitigating credit risk inherent in its commercial portfolios. Collateral for the majority of commercial loans comprises first legal charges over freehold or long leasehold property (including Companies House registration where appropriate).

For property-based lending, supporting information such as professional valuations are an important tool to help determine the suitability of the property offered as security and, in the case of investment lending, generating the cash to cover interest and repay the advance. All valuations are undertaken by members of an internally approved panel of valuers that is controlled by a dedicated team within Commercial Division.

Nationwide's standard documentation states that it has the power to have the security re-valued at the customer's expense every two years (or upon an act of default) and while a revaluation is not automatically obtained, the merits of obtaining a revaluation are considered at each facility review.

All standard documentation is subject to independent legal review and sign-off in order to ensure that Nationwide's legal documentation is robust and enforceable. Documentation for large advances is tailor-made, specifically prepared by independent solicitors, and is co-ordinated by a specialist loans documentation team to oversee all documentation issues.

A syndication strategy may be adopted to avoid large concentrations of risk and hedging strategies are considered as part of the appraisal process where borrowers have chosen fixed rates. Insurance requirements are always fully considered as part of the application process and Nationwide ensures that appropriate insurance is taken out to protect the property e.g. building or terrorism cover, and to cover an important party or to protect against an insurable event.

Treasury

Collateral held as security for treasury assets is determined by the nature of the instrument. Loans, debt securities, treasury and other eligible bills are generally unsecured with the exception of Asset Backed Securities and similar instruments, which are secured by pools of financial assets.

The Group's preferred method of documenting derivative activity is the International Swaps and Derivatives Association (ISDA) Master Agreement. It is common in such cases for a Credit Support Annex to be executed in conjunction with the ISDA Master Agreement in order to mitigate credit risk on the derivatives portfolio. Under these agreements the Group values its portfolio in-house using discounted cashflow and options pricing models as appropriate. Any such valuations are agreed with the relevant counterparties, and collateral is then exchanged in order to bring the credit exposure within agreed tolerances.

The Group's legal documentation with its counterparties for derivative transactions grants legal rights of set-off for those transactions. Accordingly, for credit exposure purposes, negative market values on derivatives will offset positive market values on derivatives with the same counterparty in the calculation of credit risk, subject to an absolute exposure of zero by counterparty.

Guarantees, from connected legal entities or Monoline insurers, may be available for some treasury counterparty debt. Where available, these guarantees may enhance the credit profile of the exposure and provide security in the event of default. Any concentration of exposures in this respect is actively monitored. Further detail about Monoline insurers can be found in the Annual Report & Accounts under Business Review – Treasury Portfolios (pages 16-18).

5.8 Credit Derivatives

The purchase of a credit derivative (credit default swap) is treated as credit substitution and enables the credit exposure to be transferred to the credit protection seller (for the future performance of contractual commitments) from the reference asset (to which exposure only arises in the joint event that the asset and the credit protection seller both default).

Currently, exposure is recorded against both the credit protection seller and the reference asset according to their relative rating. A reduction in credit exposure is recorded against the issuing counterparty. However, the total exposure remains unchanged, as part of the exposure is transferred to the credit protection seller.

At 4 April 2009, the Group had credit derivatives in place to cover the credit risk of £153 million notional (2008: £188m notional) of assets within the treasury Available For Sale portfolio. All of the credit derivatives are with US and European banking institutions rated A+ or above.

5.9 Securitisation

Retained securitisation positions

The Silverstone Master Trust programme for retail mortgages is currently the only vehicle that securitises assets originated by the Group. Notes are issued by the Silverstone Master Issuer plc to the Society, either for the purposes of creating collateral to be used for funding or for subsequent sale of notes to investors outside the Group. All of the assets pledged are retained in the Society's balance sheet. In November 2008, £1.5bn of funding was secured in this manner from the UK Government. Further detail can be found in Note 20 of the Annual Report & Accounts.

Purchased securitisation positions

The total Group exposure to purchased securitisation positions at 4 April 2009 was £7,290 million (2008: £7,063m), with mortgage-backed securities accounting for the majority of this. The following table shows the breakdown of these exposures split by credit quality steps with indicative external credit assessment ratings:

Table 17: Aggregate exposure to purchased securitisation positions

Credit Quality Step	Risk weights %		Non-granular pool	Credit assessments			Exposure Values £m
	Most senior	Base		Fitch	Moody's	S & P	
1	7	12	20	AAA	Aaa	AAA	6,452
2	8	15	25	AA	Aa	AA	366
3	10	18	35	A+	A1	A+	97
4	12	20	35	A	A2	A	167
5	20	35	35	A-	A3	A-	14
6	35	50	50	BBB+	Baa1	BBB+	76
7	60	75	75	BBB	Baa2	BBB	80
8	100	100	100	BBB-	Baa3	BBB-	8
9	250	250	250	BB+	Ba1	BB+	29
10	425	425	425	BB	Ba2	BB	1
11	650	650	650	BB-	Ba3	BB-	-
Total (Credit Quality Steps 1 – 11)							7,290
Below 11 ¹	1250	1250	1250	Below BB-	Below Ba3	Below BB-	288

¹ Deduction from capital

Further detail of securitisation can be found in the Annual Report & Accounts under Business Review – Treasury Portfolios (pages 16-18).

5.10 Counterparty Credit Risk

The Group uses derivative instruments to hedge its exposure to market risk, for example, interest rate and foreign exchange risk. Counterparty credit risk is the risk that a counterparty to a derivative instrument we hold could default. The risk is mitigated by offsetting the amounts due to the same counterparties ('Netting benefits') and by cash deposited by certain of the counterparties ('Collateral held').

The following table shows the exposures to counterparty credit risk for derivative contracts at 4 April 2009:

Table 18: Exposures to counterparty credit risk for derivative contracts

	Total £m
Interest rate contracts	2,294
Foreign exchange contracts	3,559
Other contracts	8
Gross positive fair value of contracts	5,861
Netting benefits ¹	(1,200)
Netted current credit exposure	4,661
Collateral held	(1,150)
Net derivatives credit exposure	3,511

¹ Netting benefits is after including Potential Future Credit Exposure

The net derivatives credit exposure represents the credit exposure to derivative transactions after taking account of legally enforceable netting agreements and collateral arrangements, and after including Potential Future Credit Exposure (PFCE) as required in the calculation of exposure. Included within this net exposure are amounts that relate to derivatives held in respect of the Nationwide Covered Bonds LLP which are subject to collateralisation when individual Bank credit ratings fall below certain thresholds; the same is true for material Covered Bond derivative transactions which are not already collateralised.

The Group has credit derivatives in place to cover the credit risk on £153 million notional (2008: £188m notional) of assets within the Available For Sale portfolio. All credit derivatives are purchased and have been undertaken with US and European banking institutions rated A+ or above.

International Swaps and Derivatives Association (ISDA) documentation confers the ability to use designated cash collateral to set against derivative credit exposures in the event of counterparty default. Frequent rebalancing of the collateral requirements reduces the potential increase in future credit exposure.

Collateralisation of derivatives introduces two substantive changes in the incidence of credit exposure:

- The posting of collateral reduces the impact of the current market value to the difference between the market value of the derivatives and the value of the collateral. This difference is limited by the operational use of 'thresholds' and 'minimum transfer amounts', which set criteria to avoid the movement of small amounts of collateral.
- The commitment to post collateral also shortens the timescale within which future changes in interest rates and foreign exchange rates may occur. If the counterparty fails to post additional collateral required, a default can be enforced within a very short timetable. On the assumption that operational procedures are followed, a substantial reduction in the calculation of future increases in credit exposure is permitted.

As part of its regular reporting, the Group calculates any additional requirements to post collateral in the event of a downgrade in its external rating.

Wrong-way risk may occur when exposure to a counterparty is adversely correlated with the credit quality of that counterparty. Hence, there is a tendency for the exposure to increase as the creditworthiness decreases. Where such risk arises, this is taken into account when counterparty reviews are undertaken to allow for management assessment of where appropriate mitigation is required.

5.11 Credit risk model performance

The Group received its permission to use Internal Ratings Based approaches after the start of the year covered by these disclosures. Certain comparative information is not available: estimates of expected loss against actual losses “over a longer period” and PD, LGD, and EAD outcomes against estimates. This information will be disclosed in 2010.

5.12 Model Approvals & Validation

The performance and accuracy of credit risk models is critical both in terms of effective risk management and the determination of Basel risk parameters. Probability of Default (PD) parameters are modelled to calculate risk weighted assets (RWAs) for all Internal Ratings Based (IRB) approaches. In addition, where advanced IRB approaches are used, Loss Given Default (LGD) and Exposure at Default (EAD) parameters are also modelled by the Group to determine RWAs. Models that are used to determine IRB parameters have to be reviewed and approved for first use by the FSA as part of the rollout programme.

Internal review and approval for models is carried out by the relevant risk committee (e.g. Retail Credit Risk for retail models). They are supported in this by more technical committees and a Models Group forum (which comprises managers of the modelling teams across the Group). The approval process therefore ensures that Divisional Directors, senior managers of business areas, and technical staff are involved as appropriate.

A key input to the approval process is independent model validation which is carried out by technical staff who have not been involved with building the models. This includes an evaluation of the model development and validation of the dataset used, logic and assumptions, and performance of the model analysis. Where required due to an internal materiality threshold, the Group also engages external risk management consultants to undertake independent reviews. This provides a benchmark against industry practices for consideration under the model approval process by relevant committees.

The validation results are a key factor in deciding whether a model is recommended for use. The frequency, depth and extent of the validation are consistent with the materiality and complexity of the risk being managed. The Group’s validation processes include:

- Developmental evidence: to ensure that the credit risk model adequately discriminates between different levels of risk and delivers accurate risk estimates.
- Process verification: whether the methods used in the credit risk models are being used, monitored and updated in the way intended in the design of the model. Initial testing and validation is performed when the model is developed with the performance of models being assessed on an ongoing basis.

Models are subject to regular validation monitoring and performance is reported to the relevant risk committee. If the actual performance of a model falls outside expected criteria, then it will be subject to review. All models are also reviewed annually and may be modified or recalibrated as a result.

6 Market Risks

6.1 Market Risk Overview

Market risk is defined as the potential reduction in net income, or decrease in value of the Group balance sheet, arising from adverse market movements. Specific types of market risk are listed below:

• Interest rate risk	• Basis risk	• Prepayment risk	• Attrition risk
• Foreign exchange risk	• Credit spread risk	• Access risk	

Interest rate risk arises from mortgages, savings and other financial services products offered by the Group where net interest income and the market value of the Group's assets is exposed to movements in interest rates. This risk only arises in the banking book as the Group does not have a trading book.

Foreign exchange risk arises from assets and liabilities that are denominated in a foreign currency where the Sterling value or net income may change as a consequence of variations in foreign exchange rates.

Basis risk is the risk of loss arising from changes in the relationship between interest rates which have similar but not identical characteristics (e.g. Bank of England base rate and LIBOR).

Credit spread risk arises from changes in the creditworthiness, liquidity and market risk premia for marketable instruments.

Other market risks arise when customer behaviour is different from that anticipated in respect of fixed-rate products: prepayment risk (repayment of fixed-rate mortgages), access risk (withdrawal of fixed-rate savings), and attrition risk (take-up of fixed-rate mortgages).

All market risk exposures are monitored closely and regularly reported to the Assets and Liabilities Committee (ALCO).

6.2 Interest Rate Risk

The primary market risk faced by the Group is interest rate risk. The varying interest rate features and maturities on products, together with the use of retail and wholesale funds to support these products, create interest rate risk exposures due to the imperfect matching of interest rates between different financial instruments and the timing differences of the re-pricing of assets and liabilities. Given our policy of hedging fixed-rate assets and liabilities back to floating rate, some risk arises from ALCO's decision to invest the Group's reserves according to a specified fixed-rate maturity profile. The level of risk can deviate from this (subject to limits) in particular as a result of decisions made by the Group's Treasury department to temporarily deviate from the specified fixed-rate maturity profile in the light of market conditions.

The Group manages other risks through consideration of product features and the use of appropriate financial instruments, including derivative instruments and cash instruments such as loans, deposits and bonds. The Group uses individual deterministic and variance models to calculate interest rate earnings risk arising from basis, attrition, prepayment, and access exposures. While certain exposures are subject to limits, other exposures are highlighted when appropriate for consideration of mitigation activity.

Three metrics are used to monitor interest rate risk (Value at Risk, PV01 and PV200); details of these are set out below. Limits have been set for each of these metrics to reflect the Group's low risk appetite.

Value at Risk (VaR)

This technique estimates the potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence based on historic experience. In its day-to-day monitoring Nationwide uses a 10-day horizon and a 99% confidence level.

The VaR model used by Nationwide incorporates underlying risk factors based on interest rate volatilities and correlations. Potential movements in market prices are calculated by reference to daily market data from the last two years. Exposures against limits are reviewed daily by management. Actual outcomes are monitored periodically to test the validity of assumptions and parameters/factors used in the VaR calculation.

Although a valuable guide to risk, VaR needs to be viewed in the context of the following limitations:

- VaR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.
- The use of a 99% confidence level, by definition, does not take account of changes in value that might occur beyond this level of confidence. The VaR numbers may not therefore encompass all potential events, particularly those that are extreme in nature.
- Historic data is not necessarily a reliable guide to future events.

Sensitivity analysis (PV01)

This is used to assess the change in value of the Group's current net worth against a one basis point (0.01%) parallel shift in interest rates. As is the case with VaR, this analysis is done on a daily basis separately for each currency (but with the main risk arising from Sterling exposures) and in aggregate.

Stress testing (PV200)

This is calculated in a similar manner to PV01 but against a much more severe 200 basis point (2.0%) parallel shift in interest rates. Both PV01 and PV200 numbers are generated and monitored daily.

Interest rate risk summary

The average gross Sterling exposures (before deduction of the above-mentioned benchmark profile) through 2008/09 were as follows – all exposures include investment of the Group's reserves:

Table 19: Interest rate risk exposures

	Average £m	High £m	Low £m
VaR	68.2	85.6	47.2
Sensitivity analysis (PV01)	1.9	2.1	1.5
Stress testing (PV200)	373.5	426.8	295.1

6.3 Foreign Exchange Risk

A proportion of treasury funding and investment activity is undertaken in foreign currencies and some commercial loans are denominated in Euros. Foreign currency exposure is hedged on the balance sheet or by using derivatives to reduce currency exposures to acceptable levels. In line with the prudential guidance applying to all building societies, and after taking account of foreign currency derivatives, the Group has no substantial net exposure to foreign exchange rate fluctuations or changes in foreign currency interest rates. ALCO sets limits on the level of exposure by currency; these limits are monitored daily.

VaR is used to monitor the risk arising from open foreign currency positions. Open currency positions represent the net value of assets, liabilities and derivatives in foreign currency. The parameters of the VaR methodology and frequency of reporting are exactly as described above in Interest Rate Risk (section 6.2).

At 4 April 2009, the average Sterling equivalent exposures through 2008/09 were as follows:

Table 20: Foreign exchange exposure

	Average £m	High £m	Low £m
VaR	0.2	0.5	0.0

In addition, the Group's Pillar 1 minimum capital requirement includes foreign exchange risk through the Foreign Exchange Risk Requirement FX PRR (see section 4.4).

6.4 Other market risks

All other market risks (basis risk, credit spread risk, and prepayment risk, access risk, and attrition risk) are monitored closely and regularly reported to ALCO.

Risks relating to products (prepayment risk, access risk, and attrition risk) are mitigated through appropriate restrictions in product terms and conditions, and close analysis of the product pipeline. In addition, Treasury Division uses derivative instruments in managing various aspects of market risk. In doing so it complies with the Building Societies Act 1986 which limits our use of derivatives to the reduction in exposure to changes in interest rates, exchange rates or other factors defined by the Act.

7 Operational Risk

Nationwide has adopted The Standardised Approach to operational risk and has applied the industry standard definition, namely: “the risk of loss arising from inadequate or failed internal processes, people and systems or from external events”. This has been aligned to the Group’s integrated corporate risk map and ensures that there is effective oversight, monitoring and reporting of the key operational risk exposures facing Nationwide as detailed below:

• Financial management & control	• Information technology
• Third party	• Premises & physical assets
• Fraud	• People
• Business continuity	• Customer experience
• Information security	• Legal & regulatory
• Change	

Operational Risk Framework

Oversight and governance arrangements for the setting and management of a robust operational risk management policy and culture are the responsibility of the Board, Group Risk Committee and the Operational Risk Committee. Each committee has defined Terms of Reference allocating their accountability and responsibilities.

Nationwide operates a “Three Lines of Defence” model for management of operational risk. Each division, as the first line of defence, has a dedicated operational risk officer. In the second line of defence the Group-wide network of operational risk officers is supported by a centralised Operational Risk Unit, whose role is to define and implement operational risk policies and processes consistent with corporate objectives, values and appetite.

In order to manage the Group’s key operational risks, data is captured at a divisional and risk category level from a variety of sources. These include regular control risk self-assessments, internal and external incident analysis, material losses and control failures. The information is analysed and monitored against defined risk appetite tolerances for each of the key risk categories using a central operational risk management database.

The status of the Group risk appetite metrics, significant operational risk exposures, incidents, losses and emerging trends are regularly reported to the Operational Risk Committee, Group Risk Committee and the Board to ensure transparency, and robust and effective challenge of the business.

Key operational risk categories

Responsibility for each of the key operational risk categories is allocated to a risk owner, all of whom are Directors or Senior Managers reporting to an Executive Director.

Third Party

The Group conducts its business in a fair and open manner and is committed to maximising customer value when undertaking expenditure on goods and services. Risks are monitored to ensure appropriate selection and management of third party suppliers and outsourced services, including compliance with contract law.

Business Continuity

The purpose of Business Continuity is to ensure normal business operations are maintained in the event of disruption caused by an unexpected event ensuring Nationwide:

- Maintains a safe and secure business for the benefit of our customers.
- Minimises the losses which arise from unexpected events.
- Protects the reputation of the Nationwide brand and the integrity of the UK financial services industry.

Change

It is recognised that effective change management is essential to meeting our corporate objectives. Management of this risk ensures that the Group's project and programme portfolio is aligned to Nationwide's objectives, delivered efficiently, fit for purpose and sustainable.

Customer Experience

It is essential that Nationwide delivers its customer promise by providing open, honest, good value, fair, safe and secure products and services that perform as customers have been led to expect. The purpose of this risk category is to ensure that customers can be confident that they are dealing with a firm where the fair treatment of customers is paramount, that an appropriate customer experience is consistently delivered and service levels are maintained for our customers.

Financial Management & Control

This category covers management of the risk associated with the efficient, effective and appropriate use of the Society's financial resources and their accurate recording and reporting. This includes the risk of not complying with relevant statutory and regulatory accounting and reporting requirements.

Fraud

This is the risk of direct or indirect loss resulting from intentional actions or illegal activities by people within or outside the Group. Continuing success for Nationwide depends on maintaining the trust of our customers and controlling fraud losses to minimise the impact on costs and profit.

The Group's Fraud Strategy is designed to:

- Minimise the impact of fraud losses on overall costs.
- Provide cost effective management of fraud prevention, detection and investigation.
- Create a Group wide anti-fraud culture that deters internal and external fraud.
- Meet regulatory requirements in respect of fraud management.

Nationwide combats fraud across all existing and emerging products, processes and channels, through the exploitation of technology and promoting awareness of fraud to customers and employees. This is supported by a portfolio of projects managed under the banner of the Strategic Fraud Initiative which was established in 2005 to enhance the Group's fraud prevention approach.

Information Security

Nationwide regards information as a highly valuable asset and strives to ensure that the confidentiality, integrity and availability of its information and business systems are maintained and controlled, limiting exposure to the risks arising due to loss, corruption, misuse or theft of its information assets.

Information Technology

The risk associated with the failure (or inadequate management) of technology and the data captured, stored, processed and output via that technology. This risk is managed through the Information Technology Division. Their objective is to ensure that a stable, secure and reliable IT environment is provided to support the business, and that both systems and data are secure from unauthorised access and usage.

Legal & Regulatory

As a regulated firm, Nationwide places significant importance on managing the business in a way that effectively manages the risk of fines or censure through non-compliance with laws and regulations. Oversight of Legal & Regulatory risks comprises:

- Breach of regulation.
- Breach of law.
- Breach of anti-money laundering regulations.

Nationwide identifies all material legal and regulatory requirements and relevant voluntary codes and standards affecting the Group and work with business areas to determine how it applies. This is supported by review mechanisms to ensure compliance with material regulatory and legal obligations, and a suite of Key Risk Indicators and appropriate commentary. This enables the business to monitor progress against the key legal and regulatory risk exposures and take action where we are operating outside of risk appetite.

This framework of support, challenge and monitoring:

- Enables the Board and senior management to discharge their responsibilities and satisfy legal and regulatory requirements.
- Supports the business to achieve the Corporate Plan in a compliant manner.
- Ensures relevant legislation, regulations, codes and standards are fully complied with.
- Ensures regulatory compliance is consistent and effective across the Group.
- Prevents and minimises penalties and litigation arising from non-compliance.
- Ensures reliable professional advice is sought on legal matters in order to select the optimum solutions.

People

One of Nationwide's key assets is our people. As such Nationwide is committed to ensuring that we effectively manage the risks associated with recruiting, developing, motivating, rewarding and retaining the required number of people who are competent within their role. This also includes the risk of not complying with people related legal and regulatory requirements.

Premises & Physical Assets

Nationwide ensures appropriate premises and physical assets are available to fulfil business operational needs. This means ensuring adequate, safe and secure premises are in place that conform to all relevant regulatory bodies' rules and regulations and provide a safe and healthy environment.

Glossary of terms

Basel II Accord	The Basel Committee on Banking Supervision's statement of best practice that defines the methods by which firms should calculate their regulatory capital requirements to retain enough capital to protect the financial system against unexpected losses. The Accord is structured around Pillars 1, 2 & 3, became law in the EU Capital Requirements Directive, and was implemented in the UK in the FSA Handbook.
BIPRU	The Prudential Sourcebook for banks, building societies and investment firms which forms part of the FSA Handbook for Basel II.
Counterparty credit risk	Counterparty credit risk is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows.
Credit quality steps	A credit quality assessment scale as set out in BIPRU 3.4 (Risk weights under the standardised approach to credit risk) and BIPRU 9 (Securitisation).
Credit risk	The potential to incur losses from the failure of a borrower or counterparty to meet its obligation to pay interest or repay capital on an outstanding loan.
Credit risk mitigation	Techniques to reduce the potential loss in the event that a customer (borrower or counterparty) becomes unable to meet its obligations. This may include the taking of financial or physical security, the assignment of receivables or the use of credit derivatives, guarantees, credit insurance, set off or netting.
CRR	Capital Resources Requirement – the minimum amount of capital resources that a financial institution must hold as set out in Basel II Pillar 1 rules.
Default	Circumstances in which the probability of default is taken as 100% for the purposes of the calculation of regulatory capital and compliance with Basel II. This is defined as when a borrower reaches a predefined arrears status (90 days past due for most borrowing) or where a borrower is considered unlikely to repay the credit obligation in full without the lender taking action such as realising security.
EAD	Exposure at default. A Basel II Pillar 1 parameter used to estimate the amount outstanding at the time of default.
ECAI	External Credit Assessment Institution. An ECAI (e.g. Moody's, Standard and Poor's, Fitch) is an institution that assigns credit ratings to issuers of certain types of debt obligations as well as the debt instruments themselves.
EEA parent institution	A parent financial institution situated in a Member State of the European Economic Area which is not a subsidiary of another financial institution also situated in the EEA.
Expected loss	Expected Loss, a Basel II pillar 1 calculation. The amount estimated under the IRB approach to be lost on current exposures due to potential defaults on existing and committed lending over a one-year time horizon. It is the product of PD, LGD and EAD.
Exposure	The maximum loss that a financial institution might suffer if: (a) a customer (borrower or counterparty) or a group of connected customers fail to meet their obligations; or (b) it has to realise assets or off-balance sheet positions.
Foundation IRB	Foundation Internal Ratings Based approach for measuring credit risk. This allows financial institutions to use its own estimates of PD together with standard LGD and EAD parameters.
FSA	Financial Services Authority. The financial services industry regulator in the UK.
FX PRR	Foreign Exchange Position Risk Requirement. The capital requirement under BIPRU 7 (Market risk) as part of the calculation of the market risk capital requirement included in Basel II Pillar 1.
GENPRU	General Prudential Sourcebook for banks, building societies, insurers and investment firms which forms part of the FSA Handbook for Basel II.
Guarantee	An agreement by a third party to cover the potential loss to a credit institution should a specified counterparty default on their obligations.
ICA	Internal Capital Assessment – the document produced as a result of the ICAAP.

ICAAP	Internal Capital Adequacy Assessment Process. The process the Group follows to determine capital requirements under Basel II Pillar 2.
ICG	Individual Capital Guidance. The minimum amount of capital the Group should hold as set by the FSA under Basel II Pillar 2.
Interest rate risk	Interest rate risk is the exposure of a firm's financial condition to adverse movements in interest rates.
IRB	Internal Ratings Based approach under Basel II Pillar 1 for measuring credit risks. IRB approaches are more sophisticated and risk-sensitive than the Standardised Approach. IRB may be Foundation (PD only) or Advanced (PD, EAD, & LGD). Foundation IRB is not available for retail portfolios. IRB approaches may only be used with the FSA's permission otherwise the Standardised Approach must be used.
ISDA	International Swaps and Derivatives Association is the global trade association for over-the-counter (OTC) derivatives, and providers of the industry-standard ISDA documentation.
LGD	Loss Given Default. A Basel II Pillar 1 parameter used to estimate the difference between exposure at default and the net amount of the expected recovery expressed as a percentage of EAD.
LIBOR	London Inter-Bank Offered Rate.
Long run average PD	Probability of default based on a long run average default rate which would be expected over a full economic cycle.
LTV	Loan-To-Value. The ratio of current exposure value as a proportion of the value of the asset held as security (usually residential property) expressed as a percentage.
Market risk	The potential reduction in net income, or decrease in value of the Group balance sheet, arising from adverse market movements, primarily arising from changes in interest rates.
Maturity	The remaining time in years that a borrower is permitted to take to fully discharge their contractual obligation (principal, interest and fees) under the terms of a loan agreement.
Minimum capital requirement	The minimum amount of regulatory capital that a financial institution must hold to meet the Basel II Pillar 1 requirements for credit, market and operational risk.
Model validation	The process of assessing how well a risk model performs, using a predefined set of criteria including the discriminatory power of the model, the appropriateness of the inputs and expert opinion.
Netting	The ability to reduce credit risk exposures by offsetting the value of any deposits against loans to the same counterparty.
Operational risk	Operational risk is the risk of loss arising from inadequate or failed internal processes, people and systems or from external events.
PFI	Private Finance Initiatives. Loans advanced to provide financial support for "public-private partnerships" between the public and private sectors.
PIBS	Permanent Interest Bearing Shares. Unsecured, deferred shares that are a form of Tier 1 capital. PIBS rank behind the claims of all subordinated debt holders, depositors and creditors of Nationwide.
Pillar 1 – Minimum capital requirements	The part of the Basel II Accord which sets out the regulatory minimum capital requirements for credit, market and operational risk.
Pillar 2 – The supervisory review process	The part of the Basel II Accord which sets out the processes by which financial institutions review their overall capital adequacy. Supervisors then evaluate how well financial institutions are assessing their risks and take appropriate actions in response to the assessments. This includes all risks (including Pillar 1 risks) – ICG is an outcome from Pillar 2.
Pillar 3 – Market discipline	The part of the Basel II Accord which sets out the disclosure requirements for firms to publish details of their risks, capital and risk management. The aims are greater transparency and strengthening market discipline.
PiT	Point in time. A modelling approach which assesses the credit risk of an exposure at a single point in time.

PD	Probability of Default. A Basel II Pillar 1 parameter under IRB approaches used to estimate of the probability that a borrower will default on their credit obligations in next 12 months.
Provisions	Amounts set aside to cover incurred losses associated with credit risks.
PV01/PV200	A calculation to assess the change in value of the net present value (NPV) of financial instruments with 1 basis point /200 basis points parallel shifts in interest rates. PV01 shows the sensitivity while PV200 applies a more severe stress test.
Qualifying Revolving Retail Exposures	Facilities to retail customers that provide a revolving facility e.g. credit cards and overdrafts from which credit risks arise. Nationwide's current account is the FlexAccount.
Rating system	A system for assessing and ranking customers and accounts by risk. A rating system comprises all of the methods, processes, controls, data collection and IT systems that support the assessment of credit risk, the assignment of exposures to grades or pools (rating), and the quantification of default and loss estimates for credit risk exposures.
Repurchase agreement	One party to the transaction agrees to sell securities to another and at the same time agrees to repurchase the securities at a future date for a specified price. The repurchase price will be fixed at the outset, usually being the original sale price plus an amount representing interest for the period from the sale to the repurchase.
RWA	Risk weighted assets. The value of an on- or off-balance sheet exposure adjusted under Pillar 1 rules to reflect the degree of risk it presents.
Securitisation	A transaction or scheme where assets are sold to a Special Purpose Vehicle (SPV) in return for immediate cash payment. That vehicle raises the immediate cash payment by issuing debt securities in the form of tradable notes or commercial paper to wholesale investors who receive an income from the underlying assets. Some risk is retained on the balance sheet while the remaining risk is transferred to investors. Securitisations may be purchased or retained.
Society	Nationwide Building Society.
SREP	Supervisory Review and Evaluation Process, the FSA assessment of a firm's own capital assessment (ICA) under Basel II Pillar 2.
Standardised approach	The basic method used to calculate credit risk capital requirements under Pillar 1 of Basel II. In this approach the risk weights used in the capital calculation are determined by regulators. The Standardised approach is less risk-sensitive than IRB.
Stress testing	Various techniques that are used to gauge the potential vulnerability to exceptional but plausible events.
Subordinated debt	A form of Tier 2 capital that is unsecured and ranks behind the claims of all depositors, creditors, and investing members (other than holders of PIBS).
The Standardised Approach (operational risks)	The standardised approach to operational risk, calculated using three-year historical net income multiplied by a factor of between 12-18%, depending on the underlying business being considered.
Value at Risk (VaR)	A statistical technique to estimate the maximum loss that could be made for a given factor of confidence over a set time horizon under normal market conditions.
Wrong-way risk	Defined by the FSA as a situation where there is an adverse correlation between the counterparty's probability of default and the mark-to-market value of the underlying transaction.

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